

**STATE BOARD OF EQUALIZATION
FISCAL YEAR 2010-11
PROPOSAL No. XX**

TITLE OF PROPOSED CHANGE:

Ensuring Fuel Tax Compliance

SUMMARY OF PROPOSED CHANGES:

This proposal will protect and enhance the tax base of the transportation taxes program by reducing tax evasion and increasing compliance. The Board of Equalization (BOE) requests authority to continue two successful ongoing components of the BOE's administration of the transportation taxes programs. The first component continues BOE's participation in the Joint Operations Center (JOC) Project for National Fuel Compliance which is intended to reduce tax evasion. The second component addresses the ongoing workload in the International Fuel Tax Agreement (IFTA). This component will ensure that BOE meets all of IFTA's requirements and helps BOE avoid being sanctioned. The JOC component brings in \$900,000 in federal grant money over three years and the IFTA component safeguards \$3 billion annually in federal matching funds.

The BOE requests authority to expend \$300,000 in federal funds in FY 2010-11, 2011-12 and 2012-13 to continue 2.0 three-year LT positions to participate in the JOC project and \$230,000 in FY 2010-11 and ongoing to permanently establish 3.0 LT positions to meet ongoing workload in the IFTA program. There are no new positions in this proposal and no general fund expenditures.

STATE BOARD OF EQUALIZATION**Fiscal Year 2010-11****Ensuring Fuel Tax Compliance****A. Nature of Request**

This proposal will protect and enhance the tax base of the transportation taxes program by reducing tax evasion and increasing compliance. The Board of Equalization (BOE) requests authority to continue two successful ongoing components of the BOE's administration of the transportation taxes programs. The first component continues BOE's participation in the Joint Operations Center (JOC) Project for National Fuel Compliance which is intended to reduce tax evasion. The second component addresses the ongoing workload in the International Fuel Tax Agreement (IFTA). This component will ensure that BOE meets all of IFTA's requirements and helps BOE avoid being sanctioned. The JOC component brings in \$900,000 in federal grant money over three years and the IFTA component safeguards \$3 billion annually in federal matching funds. There are no new positions in this proposal and no general fund expenditures.

JOC Project

The BOE requests the continuation of the JOC project for an additional three years which will allow adequate operational time to properly evaluate the project's impact on providing additional fuel tax revenues for the state as it transitions from its development/implementation phase to its operational phase. BOE requests authority to expend \$300,000 in Federal Highway Administration (FHWA) funds to continue 2.0 three-year limited-term (LT) positions (Business Taxes Specialist Is) for continued participation in the JOC project.

IFTA Program

BOE requests \$230,000 in FY 2010-11 and ongoing for the permanent establishment of 3.0 LT positions (1.0 Business Taxes Representative and 2.0 Tax Technician IIIs) scheduled to sunset on June 30, 2010 to meet the requirements for participation in the IFTA. Approval of this proposal will safeguard continued federal matching fuel funds by fulfilling IFTA membership agreement as well as protect the \$85.3 million revenue base that the IFTA program generates for California's Transportation Tax Fund to repair, maintain, and expand California's infrastructure, including highways, roads and bridges.

B. Background/History

BOE received resources for the JOC project initially through FY 2007-08 BCP No. 10. Due to several implementation delays including lengthy background checks required for BOE auditors, as well as the time required to format data, the project remains in the development/implementation phase. The 3.0 LT positions for the IFTA program were established in FY 2007-08 BCP No. 7 to timely process returns and send required transmittals to avoid sanctions from the IFTA community.

JOC Project

The JOC combines staff, data, and expertise from both federal and state governments to effectively identify fuel taxes under-reporting, non-reporting and trends leading to evasion. These pooled resources provide benefits to both state and federal fuel taxes compliance efforts. Combining federal and state government staff's skills and abilities increases each participant's ability to address fuel taxes compliance issues more effectively.

The JOC has established a National Data Center in the Washington D.C. area. The National Data Center is receiving and combining data from federal, state and third party sources and applying sophisticated analytical tools to the data sets to identify anomalies, inconsistencies and omissions in the data, and generate leads for JOC audit teams to follow up on in the field.

Now that the National Data Center is operational, the JOC audit teams, combining state and federal resources to conduct joint audits and investigations, are being formed and are receiving cross-training to be able to work at both the state and federal level.

Pursuant to the MOU, California has committed 2.0 positions to work full-time with the JOC. BOE staff has assisted in the development and implementation of the National Data Center, integrating California data into the National Data Center's data bases, received training with the analytical software and other tools being employed in the data center, and developed data analytic routines to compare and extract data that may be beneficial to BOE's administration of the state's fuel tax programs. Staff has also received training in federal and other states law and audit techniques, and provided similar training in California law and procedures in preparation for conducting joint audits and examinations.

In the fall of 2009 BOE will begin the analysis and investigation of the first leads being generated from the National Data Center and JOC field teams will prepare to conduct their first joint examinations.

IFTA Program

Under the Intermodal Surface Transportation Efficiency Act of 1991, a contiguous U.S. State must participate in the IFTA or the federal government will discontinue providing matching fuel funds. These funds amount to about \$3 billion annually for California. Under the IFTA, a state that does not comply with the requirements could face sanctions, including expulsion and loss of federal matching fuel funds.

The IFTA requires participating states and Canadian Provinces (collectively jurisdictions) to process tax returns and distribute funds, or send a billing to other jurisdictions by the end of the month following the month in which the return was received. The vehicle for the distribution of funds or billings to other jurisdictions is a transmittal. The IFTA also requires a transmittal to be sent to all jurisdictions each month, whether or not truckers from the base jurisdiction traveled in the other jurisdiction.

When a trucker files an IFTA return, the data is keyed and entered on the Regional Processing Center (RPC) mainframe. If the return contains errors, the RPC designates the return as being in exception status. When a return is in exception status, the BOE

cannot include the return on a transmittal until the return is verified and the exception is cleared. BOE must review all returns and clear exceptions timely to be in compliance with the IFTA.

When California joined the IFTA in 1996, staffing was based on 8,000 truckers registering with the BOE as their base jurisdiction. As of June 30, 2009, the California-based IFTA registered truckers exceeded 22,000; more than double the original number.

Each jurisdiction is evaluated by the IFTA Community for compliance every four years. BOE was cited in 2003 and 2007 for not timely transmitting monies on transmittals. BOE avoided any sanctions with the approval of 3.0 LT positions provided in FY 2007-08 BCP No. 7. BOE has been able to timely process returns and send timely transmittals since August 2007 because of these positions. In order to continue meeting the IFTA requirements, BOE requests to permanently establish these 3.0 LT positions.

C. State Level Considerations

BOE is charged by the State Constitution and by statute to oversee the property tax assessment practices of 58 county assessors, assess and allocate the property values of railroads and specified utilities, administer the state's sales and use tax, fuel, alcohol, and tobacco taxes as well as collect fees to fund numerous specific state programs. Successful administration of these tax and fee programs has resulted in the collection of 32 percent of the state's annual revenue.

The BOE collects the motor fuel taxes which are deposited in the Motor Vehicle Fuel Account with subsequent transfer to the Transportation Tax Fund and other smaller funds. The bulk of the revenue is used to support the state's transportation system. Approval of this proposal will safeguard over \$3 billion in annual federal matching fuel funds by providing staff to timely process IFTA workloads and to assist with the analysis of JOC data.

In recent years, the motor fuel reporting system at both the state and national level has moved forward rapidly to provide electronic transactions reporting. On a state level, California has developed and is already using systems to receive and analyze California data. This proposal takes advantage of rapidly expanding national fuel tax reporting by providing a national perspective to fuel tax compliance.

Approval of this proposal will also allow the Internal Revenue Service (IRS) to share fuel tax information with California. Other states and the federal government will also benefit from the proposal. The BOE, as a leader in fuel tax administration, can continue to work with these entities to improve fuel tax compliance and to deter tax evasion.

D. Justification/Analysis of Alternatives

This proposal provides an innovative approach to motor fuels tax compliance and enforcement. It leverages both state and federal resources to combine highly sophisticated data analytics with responsive, team-oriented audits of potential under-reporting and non-reporting of state and/or federal motor fuel taxes. This proposal also fulfills requirements in section 60601 of the Revenue and Taxation Code and authorizes the BOE to enforce the provisions of the Diesel Fuel Tax Law. In addition, California, as

an IFTA jurisdiction, will move toward compliance with federally mandated provisions of the IFTA. This proposal is consistent with the following BOE Strategic Plan Goals 1, 2 and 3.

- **Goal 1 – Maximize Voluntary Compliance in BOE Programs**
Strategy 5: Identify and analyze areas of noncompliance and develop approaches such as partnerships with other governmental agencies to address targeted areas of concern.
- **Goal 2 – Improve the Efficiency of BOE's Tax and Fee Programs**
Strategies 1 & 2: Create an environment that encourages innovative and creative ideas for changing and streamlining our business processes without diminishing the quality of our services or products; and identify and implement new approaches to traditional audit, collection, and return processing functions that ensure compliance with the legal requirements.
- **Goal 3 – Improve the BOE's Organizational Efficiency**
Strategy 2: Promote cooperative working relationships with other agencies, stakeholder organizations, and programs within BOE by sharing data and resources, as appropriate, to ensure the efficient use of time and resources.

Alternative 1 - The BOE requests authority to expend \$300,000 in federal funds in FY 2010-11, 2011-12 and 2012-13 to continue 2.0 three-year LT positions to participate in the JOC project and \$230,000 in FY 2010-11 and ongoing to permanently establish 3.0 LT positions to meet ongoing workload in the IFTA program. See Exhibit I (pages 9 & 10) for workload justification.

Approval of these positions will meet the current needs of both the JOC Project and the IFTA program.

Pros:

- Safeguards the estimated \$3.0 billion in federal matching fuel funds for California.
- Maintains the \$85.3 million revenue base generated by the IFTA program.
- No General Fund impact.
- Provides \$300,000 per year in federal funding earmarked for inter-governmental tax compliance initiatives to protect and enhance California highway tax revenue.
- Leverages other state and federal resources to identify evasion, non-reporting and under-reporting of California fuel tax.
- Recovers under-reported fuel taxes for California through the auditing and billing of non-compliant California taxpayers.
- Recovers California's share of federal revenue realized through the auditing and billing of non-compliant federal taxpayers.
- Provides for more efficient management and enforcement of the Diesel Fuel Tax Law and benefits honest taxpayers by providing another mechanism to assist the BOE and the federal government to maintain a level fuel tax playing field.
- Provides for the early identification of non-compliant taxpayers and newly emerging tax evasion schemes.
- Meets IFTA requirements and avoids sanctions of non-compliance.
- Enables California to meet its responsibilities to other IFTA jurisdictions.

Cons:

- Requires continuation of 2.0 three-year LT positions and permanent establishment of 3.0 LT positions.
- Reduces funds available for other intergovernmental compliance proposals received by FHWA.
- 3.0 permanent positions for IFTA will permanently reduce the monies available in the Transportation Tax Fund.

Alternative 2 - The BOE requests authority to expend \$300,000 in federal funds in FY 2010-11, 2011-12, and 2012-13 to continue 2.0 three-year LT positions to participate in the JOC project and \$230,000 in FY 2010-11, 2011-12 and 2012-13 to continue 3.0 three-year LT positions to meet ongoing workload in the IFTA program.

Approval of these positions will temporarily meet the current needs of the JOC project and the IFTA program.

Pros:

- Safeguards the estimated \$3.0 billion in federal matching funds for California.
- Maintains the \$85.3 million revenue base generated by the IFTA program.
- No General Fund impact.
- Provides \$300,000 per year in federal funding earmarked for inter-governmental tax compliance initiatives to protect and enhance California highway tax revenue.
- Leverages other state and federal resources to identify evasion, non-reporting and under-reporting of California fuel tax.
- Recovers under-reported fuel taxes for California through the auditing and billing of non-compliant California taxpayers.
- Recovers California's share of federal revenue realized through the auditing and billing of non-compliant federal taxpayers.
- Provides for more efficient management and enforcement of the Diesel Fuel Tax Law and benefits honest taxpayers by providing another mechanism to assist the BOE and the federal government to maintain a level fuel tax playing field.
- Provides for the early identification of non-compliant taxpayers and newly emerging tax evasion schemes.
- Meets IFTA requirements and avoids sanctions of non-compliance.
- Enables California to meet its responsibilities to other IFTA jurisdictions.

Cons:

- Continues 5.0 LT positions for three years.
- Reduces funds available for other intergovernmental compliance proposals received by FHWA.
- 3.0 permanent positions for IFTA will temporarily reduce the monies available in the Transportation Tax Fund.
- Does not allow BOE to meet IFTA ongoing workload requirements beyond the tenure of the LT positions and requires BOE to request additional continuation of the IFTA positions when they expire.

Alternative 3 – BOE requests \$230,000 in FY 2010-11 and ongoing to permanently establish 3.0 LT positions to meet ongoing workload in the IFTA program.

Approval of this alternative will meet the current needs of the IFTA program only. This alternative does not meet the current needs of the JOC project.

Pros:

- Safeguards the estimated \$3.0 billion in federal matching funds for California.
- Maintains the \$85.3 million revenue base generated by the IFTA program.
- No General Fund impact.
- Meets IFTA requirements and avoids sanctions of non-compliance.
- Enables California to meet its responsibilities to other IFTA jurisdictions.
- Provides for more efficient management and enforcement of the Diesel Fuel Tax Law and benefits honest taxpayers by providing another mechanism to assist the BOE and the federal government to maintain a level fuel tax playing field.
- Eliminates the 2.0 LT positions for the JOC Project.
- The FHWA funds currently being received by BOE can be reallocated by FHWA to other states' intergovernmental compliance proposals received by FHWA.

Cons:

- Turns down \$300,000 per year in federal funding earmarked for inter-governmental tax compliance initiatives to protect and enhance California highway tax revenue.
- Does not leverage other state and federal resources to identify evasion, non-reporting and under-reporting of California fuel tax.
- Reduces the state's ability to recover under-reported fuel taxes for California through the auditing and billing of non-compliant California taxpayers.
- Places at risk California's share of federal revenue realized through the auditing and billing of non-compliant federal taxpayers.
- Reduces the ability for the early identification of non-compliant taxpayers or newly emerging fuel tax evasion schemes.
- Does not allow California to benefit from the expertise of other states and the IRS in analyzing data and performing audits.
- 3.0 permanent positions for IFTA will temporarily reduce the monies available in the Transportation Tax Fund.

E. Facility/Capital Outlay Considerations

Since this proposal requests continuation and permanent establishment of positions previously authorized on a limited term basis there is no additional impact on existing facilities.

F. Outcomes and Accountability

JOC Project

Approval of this proposal will result in staff's continued participation in the JOC Project which will result in less tax evasion. Staff will continue to participate in data analytics under the direction of the National Data Center, and participate in joint audits and examinations resulting from leads generated by the National Data Center. Results will be accumulated and increased revenue for California will be identified. Since the JOC

will maintain a full accounting of their efforts, the results will be easily captured and measured to provide accountability.

IFTA Program

This proposal keeps the size of the existing Motor Carrier Section return processing program elements stable to ensure compliance with the IFTA. Processing of IFTA returns, billing and collecting amounts due, and resolution of delinquent and revoked accounts will be calculated and compared to prior years to verify compliance with the IFTA.

G. Timetable

Implementation of this proposal is shown by Fiscal Year in the table below.

FY2010-11	FY 2011-12	FY 2012-13
Joint Operations Center <ul style="list-style-type: none"> Conduct joint federal/state audits and investigations. IFTA Program <ul style="list-style-type: none"> Process IFTA tax returns Clear exceptions Timely send transmittals 	Joint Operations Center <ul style="list-style-type: none"> Continue to conduct joint federal/state audits and investigations. IFTA Program <ul style="list-style-type: none"> Process IFTA tax returns Clear exceptions Timely send transmittals 	Joint Operations Center <ul style="list-style-type: none"> Continue to conduct joint federal/state audits and investigations. Evaluate program activities and impact of operations. Based on evaluation of program, develop BCP to continue program, if warranted.
		FY 2012-13 and Ongoing
		IFTA Program <ul style="list-style-type: none"> Process IFTA tax returns Clear exceptions Timely send transmittals

H. Recommendation

Alternative 1 is recommended. The BOE requests authority to expend \$300,000 in federal funds in FY 2010-11, 2011-12 and 2012-13 to continue 2.0 three-year LT positions to participate in the JOC project and \$230,000 in FY 2010-11 and ongoing to permanently establish 3.0 LT positions to meet ongoing workload growth in the IFTA program.

Approval of this proposal will best meet the current needs of the JOC project and the IFTA program. In addition, BOE will meet the IFTA requirements and safeguard the estimated \$3.0 billion in matching federal funds and maintain \$85.3 million in revenue

generated by the IFTA program for the continuation of repairs, maintenance and expansion of California's infrastructure, including highways, roads and bridges.

Both the federally funded JOC project and the IFTA program are designed to increase fuel tax compliance throughout the nation. California will benefit several ways. First, when it identifies non-compliance within California and second, when federal non-compliance is identified. California receives approximately 10% of all federal fuel tax revenues apportioned to the states for transportation projects.

I. Fiscal Detail

See attached "Fiscal Detail" schedules.

DRAFT

Fuel Taxes DivisionEXHIBIT I
(Page 1 of 2)**JOC Project Workload Justification****Business Taxes Specialist I (BTS I)**

The Business Taxes Specialist I conducts audits and investigations and performs data analysis of the JOC audits. The chart below summarizes the workload hours required for the Business Taxes Specialist I positions in FY 2010-11 and ongoing:

Workload Activity	Hours per Occurrence	Occurrences per Year	Total Hours
Auditing & Investigation	200	12	2,400
Data Analysis	4	200	800
Total BTS I Hours			3,200
Total BTS I Positions Requested (1,600 Hours per Position)			2.0

Fuel Taxes DivisionEXHIBIT I
(Page 2 of 2)**IFTA Program Workload Justification****Business Taxes Representative (BTR)**

The BTR performs routine IFTA compliance activities including enforcement activities, verification of credentials, collection of amounts due, resolution of revocations, verification of refunds, assessment of penalties, correspondence with truckers regarding return preparation issues, and preparation of billings based on reviews. All of these activities are in support of preparation of transmittals and billings to other jurisdictions or sending billings to truckers.

Workload Activity	Hours per Occurrence	Occurrences Per Year	Total Hours
Verify credentials	.07	2,742	192
Issue penalty determinations	1.25	25	31
Collect Accounts Rec. amounts due	6.0	100	600
Review returns and correspond with truckers	.25	4,000	1,000
Total BTR Hours			1,823
Total BTR Positions Requested (1,800 Hours per Position)			1.0

The table below summarizes the workload hours required for the BTR position in FY 2010-11 and ongoing:

Tax Technician (TT III)

The TT III prepares online IFTA billings for taxes and penalties due, processes refunds of overpayments, and handles the more difficult registration and return analysis functions. The chart below summarizes the workload hours required for the TT III positions in FY 2010-11 and ongoing:

Workload Activity	Hours per Occurrence	Occurrences per Year	Total Hours
Online billings, refunds & adjustments	.5	6,000	3,000
Registration & account maintenance	1.2	116	140
Complex return analysis actions	1.0	500	500
Total TT III Hours			3,640
Total TT III Positions Requested (1,800 Hours per Position)			2.0

BCP No.
DATE: August 31, 2009

STATE OF CALIFORNIA
BUDGET CHANGE PROPOSAL--FISCAL DETAIL
STATE OPERATIONS
FISCAL YEAR 2010-11
(Dollars in Thousands)

Title of Proposed Change: ENSURING FUEL TAX COMPLIANCE

Program/Element/Component: 50 Transportation Fund Tax Program/All Elements

PERSONNEL YEARS

	CY 2009-10	BY 2010-11	BY + 1 2011-12	CY 2009-10	BY 2010-11	BY + 1 2011-12
TOTAL SALARIES AND WAGES _a/		5.0	5.0		\$275	\$275
Salary Savings		-.3	-.3		-14	-14
NET TOTAL SALARIES AND WAGES		4.7	4.7		261	261
Staff Benefits _a/					95	95
Distributed Administration _b/					39	39
TOTAL PERSONAL SERVICES					\$394	\$394
OPERATING EXPENSE AND EQUIPMENT						
General Expense					\$12	\$12
Distributed Administration					10	10
Printing						
Communications					4	4
Postage						
Travel--In-State					11	11
Travel--Out-of-State					34	34
Training					4	4
Facilities Operations					52	52
Consulting & Professional Services: Interdepartmental						
Consulting & Professional Services: External						
Department of Technology Services					8	8
Data Processing					1	1
Equipment						
Other Items of Expense: (Specify Below)						

_a/ See page 14 of 14 for itemized staff benefits and classification detail.

_b/ Represents Distributed Administration costs resulting from this BCP. The Distributed Administration costs for existing BOE programs will reflect a corresponding decrease which will be addressed in the Planning Estimate process.

		BCP No.		
		CY 2009-10	BY 2010-11	BY + 1 2011-12
TOTAL OPERATING EXPENSE AND EQUIPMENT			\$136	\$136
TOTAL EXPENDITURES (State Operations)			\$530	\$530
<u>Source of Funds</u>				
General Fund	(0001)			
Special Funds:				
Breast Cancer Fund	(0004)			
State Emergency Telephone	(0022)			
Motor Vehicle Fuel Account	(0061)		230	230
Occupational Lead Prevention Fund	(0070)			
Childhood Lead Poisoning Prev. Fund	(0080)			
Cig. and Tobacco Prod. Surtax Fund	(0230)			
Oil Spill Prevention and Admin. Fund	(0320)			
Integrated Waste Management	(0387)			
Underground Storage Tank Fund	(0439)			
Energy Resources Programs Account	(0465)			
CA. Children and Families First Trust Fund	(0623)			
Federal Trust Fund	(0890)		300	300
Timber Tax Fund	(0965)			
Gas Consumption Surcharge Fund	(3015)			
Water Rights Fund	(3058)			
Elec. Waste Recovery and Recycling Acct.	(3065)			
Cig. and Tobacco Prod. Compliance Fund	(3067)			
Federal Funds				
Other Funds				
Reimbursements	(0995)			
Net Total Augmentation (Source of Funds)			\$530	\$530

**DETAIL OF STAFF BENEFITS
AND PERSONAL SERVICES**

Staff Benefits Detail:

	CY 2009-10	BY 2010-11	BY + 1 2011-12
	(Whole Dollars)		
OASDI		\$19,967	\$19,967
Health Insurance		34,567	34,567
Retirement		38,701	38,701
Workers' Compensation		157	157
Industrial Disability Leave		224	224
Non-Industrial Disability Leave		201	201
Unemployment Insurance		131	131
Other		877	877
TOTAL		\$94,824	\$94,824

Classification	Positions			Salary Range	a/	Amount		
	CY 2009-10	BY 2010-11	BY + 1 2011-12			CY 2009-10	BY 2010-11	BY + 1 2011-12
Property & Special Taxes Department								
Motor Carrier Section								
Business Taxes Rep (LT to P)		1.0	1.0	\$42,384			\$42,384	\$42,384
Tax Technician III (LT to P)		2.0	2.0	39,036			\$78,072	\$78,072
Fuel Industry Section								
Business Taxes Sp I (3yr LT)		2.0	2.0	77,424			\$154,848	\$154,848
Blanket Funds:								
Overtime (Various)								
Temporary Help								
TOTAL SALARIES AND WAGES		5.0	5.0				\$275,304	\$275,304

_a/ The salary is the mid-step of the salary range for the stated classification.